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Ms. Eileen Donovan
Acting Secretary
Commodity Futures Trading Commission
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COMMENT

Re: Regulatory Governance

Thank you for the opportunity to comment on your proposal for Acceptable Practices under Core Principle 15 of the Commodity Exchange Act.

I am happy to respond because I think I have practical experience that is important to consider. I was Chairman of the Chicago Board of Trade ("CBOT") from 2001-2003, served on its Board of Directors and the executive committee thereof from 2001-2006, and was the Audit Committee Chairman when the CBOT became a public corporation.

In addition, I have experience with the corporate governance models of securities exchanges as I served on the nominating committee for the Board of Directors of the Chicago Board Options Exchange in 2005-06. Finally, as a management consultant with McKinsey & Company and as a corporate attorney, I worked with corporate boards generally.

My comment will consider only one aspect of your proposal, whether mere membership in the contract exchange should be a disqualifier to being a "public" director. Commissioner Fred W. Hatfield has raised important questions about this proposal and I endorse his views.

You should know that I am speaking from the perspective of a CBOT shareholder and futures trader (I retired as a director in May and have no plan to resume such activity). As a shareholder and active futures trader, I want people on the Board who understand markets and have substantial shareholdings that they have purchased themselves. I have the same attitude toward any other company I own shares in: knowledgeable directors with financial stakes.

Based upon my practical experience with exchanges and corporate governance generally, I think it would be a serious mistake to say that a director cannot be "public" simply because he is "a member of the exchange, or a person employed by or affiliated with a member". As a "bright line" test, this is much too broad and would exclude from the Board people that have both industry knowledge and substantial shareholdings in the enterprise.

Directors from outside the industry have substantial value, just as they do on boards of other public companies. However, trading rules and procedures are so complex (algorithms, black box trading, millisecond differentials, etc.) that such directors have great difficulty in understanding the issues.

In addition, there is such diversity in the derivatives markets operated by the CBOT or CME (e.g., interest rates, stock indexes, agriculturals, currencies, futures, options on futures, binary options, etc.) that the Board needs members that together have a wide variety of industry experience. The proposed Acceptable Practices would reduce the number of industry knowledgeable directors and as a market participant, I would have less confidence in such a Board.

It is true that there are industry people who are not members that could be drawn upon. But again a practical point: it is the members of the contract exchange that have the interest and enthusiasm to be directors in today's corporate environment. Good directors are hard to find and recruit and this proposal would reduce the number available substantially.

Displacing the number of industry knowledgeable people on executive committees would be even more of a serious mistake.

The executive committee of the CBOT generally meets at least once per month and so is more "hands on" than the Board itself. Fifty percent "public" representation would replace members with industry knowledge. This could mean, in the case of the CBOT, the loss of three people with industry and market experience from its executive committee, leaving only two (on the overall Board, there would be a loss of four to five people).

The consequence would be less informed discussion and therefore the likelihood of worse decisions. You should know that is people with industry experience that can challenge and improve exchange management, and the forced replacement that would be a consequence of this proposal would not be good for the public or the shareholders.

So my first point is that a blanket rule excluding member directors as "public" would have clear costs. Against these costs I see very little benefit as I believe the

"reduction of conflicts" arguments are based on improbable "what ifs" that have not occurred to date nor are likely to occur in the future..

Let me address two arguments used in the Acceptable Practices proposal:

1. Are today's challenges to self regulation greater than those in the past, e.g., would the regulatory budget be subject to cut by for profit exchanges?

   In my six years on the Chicago Board of Trade Board, there was never an instance in which the budget for regulatory activities was challenged or questioned and this was true even during the relatively lean financial year of 2001. This is not an area where we look to save money.

   The CFTC does an excellent job in monitoring exchange regulatory activities and any shortfalls are addressed and corrected. This is a day-to-day management issue such that, while the Board is responsible for oversight, proper compliance does not depend on Board composition.

   Further, the attitude of the member directors I have known is that the product we provide to customers is fair, open and transparent markets and critical to this is effective regulation. Consequently, the proposition that members on a Board would cut the regulatory budget for the sake of short-term profit is simply not a realistic argument.

   Corporations generally – whether food companies, utilities, manufacturing, etc. – have public responsibilities. All could "hypothetically" cut regulatory or safety expenses because of shareholders on their boards. Yet no one would consider this an argument that shareholders are suspect or less worthy as directors.

   It is true that for profit exchanges are both commercial and self-regulating organizations and so are different than companies generally, i. e., they have special responsibilities. . However, these exchanges also have the benefit of regular rule enforcement reviews from its regulator, in addition to corporate governance standards, requirements of Sarbanes-Oxley, and the general responsibilities and obligations that go with being a listed public company.

   Finally, and most importantly, what exchanges exist for and what they "sell" is credibility. Their brand is fair, open and transparent markets. To damage that brand by weakening regulation would be foolish and would destroy the value of the exchange. Consequently, I believe that the

"pressures" of for profit status provide greater regulatory assurance, not less. .

Commissioner Hatfield asked these very appropriate questions: (1) is there an existing problem that this proposal addresses, and (2) is there any evidence that this proposal would provide greater regulatory assurance. My answer to both questions is "No;" self-regulation has worked well in the past and for profit status will assure continued strong self-regulation in the future.

2. Are member directors so prone to conflicts that they would impair proper Board functioning?

While serving in my positions at the CBOT, I worked with twenty or more member directors. All were aware of and observed conflict of interest rules. In general, they were extremely scrupulous in stating how they might be affected by a decision and either recused themselves or voted AGAINST their perceived position. But the most important thing is that conflicts HARDLY EVER came up. There are just not that many Board decisions that affect individual board members to any significant degree.

John Damguard of the FIA has argued for this disqualification of members as public directors on the basis that top executives of major FCM firms have such major responsibilities to their clients and firms that it would be difficult for them to overcome "a serious public perception of a conflict of interest, robbing even sound exchange decisions of the credibility and market acceptance they deserve (Comment Letter of January 23, 2006)."

I agree with John that the expertise and counsel of these top executives is better gotten through other channels than the boardroom..

But this is a very limited group of members and considerations concerning them should not become the basis for a blanket rule.. The CBOT has thousands of members, many of whom are retired and lease memberships to others. Most do not have the market presence (the futures industry is so large and traders so numerous that very few traders are so active that they affect the market). Nor do they have the executive positions with large firms that create real or perceived conflicts. .

Since becoming public, corporate governance standards have become strict and more formalized. All directors must provide comprehensive information on their exchange activities. The general counsel monitors

compliance with the conflict of interest policy, and reports to the Board should there be an issue.

Finally, as a public corporation, it would be seriously destructive to allow conflicts to influence actions, both because of CFTC enforcement as well as shareholder suits.

So I consider the "possibility of conflicts" issue to also be an unrealistic argument. Consider the self-discipline of conscientious directors, the review by general counsel, the corporate governance standards, an alert regulator in the CFTC, the presence of the outside directors on the Board NOW, the possibility of litigation and finally, the fact that market participants outside the boardroom watch exchange decisions carefully.

We have many layers of protection and review today that build upon what has been an already excellent regulatory record.

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In conclusion, I agree with the concern expressed by Commissioner Hatfield that

> "the Board Composition proposal ... would create an additional and perhaps unnecessary layer of regulation for publicly traded exchanges, which are already subject to myriad new and enhanced corporate governance requirements, including, among others, Securities and Exchange Commission registration requirements, the audit committee provisions of the Sarbanes-Oxley Act of 2002, and the listing standards of the New York Stock Exchange (NYSE). I agree that the dual function of exchanges as commercial enterprises and self-regulatory organizations sets them apart from corporations engaged in business for the sole purpose of earning profits for the benefit of shareholders. In my opinion, however, the foregoing corporate governance standards, combined with properly structured ROCs and disciplinary committees, and the Commission's continuing obligation to monitor exchanges through rule enforcement reviews and otherwise, have provided multiple levels of safeguards that should be sufficient to ensure that exchanges' self-regulatory obligations are not compromised."

Consequently, I would ask that you reconsider and withdraw the recommendation that membership status alone is a disqualifier for "public" directors.

Very truly yours,

Nickolas J. Neubauer